

BUSINESS AVIATION IN UKRAINE

Summary

Ukraine's market of business aviation is small but offers good prospects for growth in the next decade. Business aviation has carved its own niche in an air transport market that did not previously exist. An inefficient and rapidly aging fleet of private aircraft currently in use offer good opportunities for US suppliers of aviation technology. An undeveloped infrastructure for private aviation creates a niche for airport developers and service companies. Leasing and financing schemes will also be in demand as the market develops. Excessive regulation and non-transparency in ownership are the two negative factors in the development of the business aviation market.

Market Overview

The business aviation market is relatively small in Ukraine. While no official statistics in the "business or private aviation" segment is available, market insiders estimate the market size to be in the range of \$30 to \$40 million in 2004 (services only, excluding the cost of airplanes.).

Charter aviation companies dominate the local market, experiencing no foreign competition. The largest local airlines involved in business aviation are: Challenge Aero, Business Aviation Center, Aero Charter, Aero Star, Ultra In-Flight, Business Airlines (Ukrprominvest Group), CABI (Donetsk), UES Avia and YuzhmashAvia (Dnipropetrovsk).

The Ukrainian Civil Aviation Authority – State Service of Ukraine for Aviation Safety Oversight (Derzhaviasluzhba) – makes no official designation for "business aviation" or "aircraft used for business aviation." The term used in Ukraine is rather broad – "the aviation of general purpose." More than 50 airplanes were used for business aviation in 2004/2005.

Market Trends

During 2002-2005 the business aviation sector demonstrated an impressive growth of 20% to 25% each year. It is expected that this trend will continue at the same pace in the next five years. With the expansion of the European Union now bordering Ukraine in the west, many western corporations already started to look at Ukraine as a cost-effective alternative to European manufacturing. The demand for corporate aviation will increase as foreign investment grows.

Poor development of domestic aviation services caused by the economic crises of the 1990s offers an additional advantage for business aviation and aero-taxi in Ukraine. Scheduled commercial flights are available between Kyiv and major oblast administrative centers only (Donetsk, Dnipropetrovsk, Simferopol, Odessa, Kharkiv, Lviv, Ivano-Frankivsk, Chernivtsi), but no commercial flights exist between oblast centers. For example, it is impossible to fly directly from Kharkiv to Odessa, the second and third largest Ukrainian cities (over 1,000,000 of population each) by commercial airlines. This may offer good opportunities for aero-taxi services.

To date, no business aviation facility such as separate terminals and hangars exist at Ukrainian airports, although regional airports such as Kyiv-Zhuliany (IEV), Lviv (LWO), and Belbek (UKS) in Crimea have ambitious plans to develop such facilities. By October 2005, Kyiv-Zhuliany Municipal Airport and Turkish TAV Group announced a project for developing a modern business aviation terminal at the existing facilities of Kyiv-Zhuliany. Because of long curfew hours (in some airports from 8:00 PM till 6:00 AM) and outdated navigation equipment, many regional airports may not be acceptable for business aviation clients.

Few Ukrainian corporations own and use private airplanes for business use. However, international business expansion of some of the Ukrainian industrial groups generate a demand for corporate jets. In 2005, two Donetsk-based business groups – System Capital Management, and Donbass Industrial Union – acquired large industrial assets in Poland, Hungary and the Slovak Republic. Two other Dnipropetrovsk-based groups – Privat, and Interpipe – own industrial properties all over Ukraine and in neighboring states, thereby being preferred customers with business aviation operators.

Competition

The Russian designed jet Yakovlev-40 (YK4) is the main “working horse” in the Ukrainian business aviation market. Thirty-two YK4 jets (10-17 seats) were used in business aviation in 2005. However, the obsolescence of these aircraft and low fuel efficiency make Ukrainian private jet owners switch to western technology. The average age of the YK4s used in Ukraine is 25-30 years. Ten YK4 jets (out of 32) have to be phased-out by 2009, and another 13 by 2012.

The fuel consumption rate of a YK4 is 65-70 % higher than a Beejet-400 or a Learjet-60. Rapidly growing prices for jet fuel make Russian aircraft extremely inefficient. The market price for jet fuel in Ukraine grew by over 27% for nine months of 2005 from \$663 per ton in January 2005 to \$840/ton in September 2005. In addition, YK4 is no longer allowed to fly to EU countries because the jet is not consistent with EU emission and noise requirements. This significantly limits the operational routes by Ukraine and CIS states.

So far, no Russian-designed business aircraft is in serial production. Therefore, there are few options for Ukrainian air taxi or corporate operators but to equip themselves with modern western business jets. US suppliers of business aviation technology may consider these market advantages in Ukraine:

By September 2005, the following business jets were operated by local business/charter airlines:

- Yakovlev-40 – 32 jets. The largest operators are: Challenge Aero, Aero Charter, and Aero Star.
- Falcon-20 – two jets with Ukrainian registration, and two jets with Russian registration.
- Falcon-50 – one jet (Ukrainian registration).
- Beejet-400 – one jet (foreign registration).
- Learjet-60 – one jet (foreign registration).
- Hawker-800 – two jets (foreign registration).
- Falcon-2000 – two jets (foreign registration, privately owned).
- Challenger-601 – one jet (foreign registration, privately owned).

- Bombardier Global Express – one jet (foreign registration).
- BBJ (Boeing727) – one jet (foreign registration).
- Bell430 VIP – one helicopter (Ukrainian registration, used by government).
- Bell407 – two helicopters (foreign registration).
- Beechcraft King Air350 – two jets (Ukrainian registration, used by government).
- Antonov-74TK-300 – two jets, used by government.

Market Access

Complicated and burdensome certification and high import duties are the two main deterrents making a critical impact on a U.S company's ability to successfully enter the Ukrainian business aviation market. It could take up to three years and hundreds of thousands of dollars to go through a type certification. Imports of foreign aircraft are subject to import duty and value-added taxation that adds another 30% to the cost of aircraft.

The State Service of Ukraine for Aviation Safety Oversight (Derzhaviasluzhba) is the Ukrainian civil aviation authority responsible for type certification. According to Derzhaviasluzhba, the following types of foreign aircraft have valid Ukrainian certificates:

1. Boeing 737 series 200, 300, 400, 500; Boeing 767-300ER.
2. McDonnell Douglas 82 and 83.
3. Super King Air-350.
4. Falcon-20, Falcon-50, Falcon-60, Falcon FAN-Jet Series C, D, E, F.
5. Airbus 319-113; 319-114; 319-131; 319-132; 319-133; 320-111; 320-211; 320-212; 320-231; 320-232; 320-233.
6. Bell 430, Bell 407 helicopters.
7. Schweizer 269C, 269C-1 helicopters.

The ownership of most foreign-made aircraft used in Ukrainian business aviation is extremely non-transparent. Complicated type certification procedures multiplied by inconsistent taxation regulations force many business aviation providers to look for alternative ways of property management. A popular scheme that many local business aviation providers use is registering a temporary entry title of a foreign jet on a private individual. This offers "certification and tax free use" of an airplane for up to 12 months with a possible extension after re-entry. Some business aviation and charter airlines, especially those associated with certain "industry oligarchs" receive aircraft as an in-kind charter fund contribution of a foreign co-founder or investor, in most cases an off-shore company owned by the same individual. It is not unusual to see an airplane under the registration of Aruba or Cyprus but operated by a local company in Ukrainian airports.

Market Entry

As in any foreign country, a local partner or representative can provide valuable insight and commercial intelligence that might otherwise be missed by the U.S. businessperson. A local representative can be especially helpful in newly emerging markets, where a strong business information network has yet to develop.

One advantage of dealing with agents and distributors is that they can handle the often cumbersome certification and license procedures for imported products. Problems have arisen for U.S. companies that sell through their Euro zone subsidiaries or distributors.

Unfavorable currency exchange rates and higher European taxes and/or duties decrease the price competitiveness of U.S. products. Additionally, working through European subsidiaries is perceived by Ukrainian businesses as an additional layer of bureaucracy and overhead cost. Ideally, a U.S. company interested in conducting a successful business operation in Ukraine should have an in-country representative and an established network of distributors and sellers.

However, before entering a distributorship or agent agreement, U.S. companies are advised to keep the following points in mind:

- 1) While the extent of information on Ukrainian companies has improved slightly, there is still a significant dearth of background data and credit history on potential Ukrainian distributors. This presents the greatest obstacle to finding reliable, competent distributors. In order to obtain a due diligence report on a potential Ukrainian partner, a U.S. company is advised to contact either a law firm or market entry facilitator. Please refer to <http://www.buyusa.gov/ukraine/en/page30.html>). U.S. companies may also purchase an International Company Profile (ICP) from the U.S. Commercial Service (CS Kiev). For details, see <http://www.buyusa.gov/ukraine/en/8.html>.
- 2) To find a potential partner, U.S. companies may wish to use the U.S. Embassy's Commercial Service programs: the International Partner Search (IPS) and Gold Key Service (GKS). For details, see <http://www.buyusa.gov/ukraine/en/8.html>.
- 3) The Embassy strongly advises that all U.S. companies consider legal counsel before and while doing business in Ukraine. Given the tenuous commercial environment and weak legal infrastructure, it is essential to obtain solid legal advice in structuring your company's investment. Furthermore, it is important to keep-up with the changing laws and regulations. Legal counsel can provide general advice on fluctuations in the commercial environment in Ukraine and prevent disputes from emerging between partners in the future.
- 4) It is typical for Ukrainian companies to seek to establish long-term business relations on consignment or on an equal investment-sharing basis. U.S. exporters are advised to start with small sales and full prepayment or letter of credit terms. U.S. exporters should be cautious about any balance payments, due to constantly changing rules on local banking procedures.
- 5) Kiev is not the only hub of trade in Ukraine. Look for distributors that have nationwide capabilities, including the major regional cities of Lviv, Odessa, Zaporizhzhya, Dnipropetrovsk, Donetsk, and Kharkiv. These regions are considered important industrial centers of Ukraine and are densely populated.

Key Contacts

Contact information about key industry players, industry publications, websites, and organizers of trade shows and trade promotion events related to this report is provided solely for interested U.S. companies upon request to CS Kiev or Commercial Service Export Assistance Centers located in major U.S. cities (see www.export.gov for Export Assistance Center addresses). American companies are welcome to send their requests to the Export

Assistance Centers with a copy to: Yuriy Prikhodko, CS Kiev Commercial Specialist, e-mail: Yuriy.Prikhodko@mail.doc.gov; The Commercial Service, U.S. Embassy Kiev, 4 Hlybochytska St., Kyiv 04050, Ukraine, Tel: (380-44) 490-4018; fax: (380-44) 490- 4046).

Upcoming Trade Shows/events

For a listing of trade shows taking place in Ukraine see <http://www.expoua.com>.

Major local trade show organizers and fair authorities include: PremierExpo (www.pe.com.ua), Euroindex (www.euroindex.com.ua), ACCO International (www.acco.com.ua), International Exhibition Center (www.iec-expo.com.ua), and KievExpoPlaza (www.expoplaza.kiev.ua). CS Kiev actively promotes American exporters at the major local trade shows, organizing and staffing U.S. Product Literature Centers at the shows (see <http://www.buyusa.gov/ukraine/en/28.html>).